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NO.

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Supreme Court
of the
United States
October Term, 1985

IN THE MATTER OF: CUSATO BROTHERS INTERNATIONAL, INC., BANKRUPT
JAMES B. McCRACKEN, TRUSTEE AND STATE OF FLORIDA,

Petitioner,

vs.

GREAT AMERICAN BANK OF BROWARD COUNTY,

Respondent.

RESPONSE TO PETITION FOR WRIT OF CERTIORARI DIRECTED TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

Respectfully submitted,

by MARY ELLEN SHOEMAKER, ESQ.
REGGIE DAVID SANGER, ESQUIRE
208 S.E. 9th Street
Fort Lauderdale, FL 33316
(305) 463-8547

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SUMMARY OF THE ARGUMENT

There is no need for this Court to resolve any conflicts between the Twenty-first Amendment and the Bankruptcy Clause as there are Federal statutes which have already resolved the conflict; by statute the Bankruptcy Trustee is liable for State taxes only where he is actually conducting the business, not liquidating the business.

The holding in the Eleventh Circuit does not conflict with either *Swarts vs. Hammer*, 194 U.S. 441 (1904) or with *Ashton vs. Cameron County Water Improvement District*, 298 U.S. 513 (1936). Neither case involves a liquidation sale by a bankruptcy trustee. *Ashton* involves a water district, a political subdivision of California, which sought the protection of the Bankruptcy court for relief from its creditors. *Swarts* involves the Trustee's obligation to pay state property tax for personal property in his custody.

Finally, there is no conflict among the Circuits as to whether state taxes are due when a Trustee liquidates inventory. The Petitioner claims that in the Second, Third, Fifth, Seventh and Eighth Circuits taxes would be imposed on the Trustee. The Petitioner cites one case for each Circuit, but each case can be distinguished from the case at bar. Both the Second Circuit and the Fifth Circuit cases involve a very narrow situation in which the primary liability for the tax is on the purchaser at the liquidation sale and not on the seller/Trustee. That is not the situation in the case at bar.

Both the Third Circuit and Seventh Circuit cases involve taxes imposed during the time the Trustee was

operating an ongoing profitable business, not when he was liquidating inventory. Further, both cases involve the payment of Federal taxes, not State taxes as in the case at bar. Finally, the Eighth Circuit case involves a state statute which specifically makes a Trustee in bankruptcy liable for unemployment taxes.

The Eleventh Circuit does not stand alone in prohibiting taxation of liquidation sales. In the Ninth Circuit, if the Trustee is not operating the business but merely liquidating inventory, no tax will be imposed.

ARGUMENT I

ANY CONFLICT BETWEEN THE TWENTY-FIRST AMENDMENT AND THE BANKRUPTCY CLAUSE HAS BEEN RESOLVED THROUGH FEDERAL STATUTE, AND DOES NOT NEED TO BE RESOLVED BY THIS COURT

The Petitioner argues that there is a conflict between the Twenty-first Amendment and Congress' power under the Bankruptcy Act, and that the conflict should be resolved by this Court. The Eleventh Circuit did not address the Twenty-first Amendment in its decision.

Rather the Eleventh Circuit relied on Federal statutes to determine whether tax liability should be imposed at a liquidation sale. First, a Trustee is required to manage and operate property within his possession according to applicable State law. 28 U.S.C. §959(b)(1978).* Second, any officers conducting business under the authority of the United States Court are subject to

*28 U.S.C. §959(b) (1978)

> A trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

taxes when they are conducting the business. 28 U.S.C. §960. (1948).**

The legislative history of 28 U.S.C. §960 shows that Congress intended the tax liability to be the same for a Trustee conducting the business under court order as it would have been had the owner continued to *possess and operate* the business. *Palmer vs. Webster*, 312 U.S. 156, 162 (1948) citing 28 U.S.C. §124a, the former §960 (emphasis added).

But where a Trustee conducts a liquidation sale of the debtor's assets, he is not conducting a business under the purview of 28 U.S.C. §960 (1948). *In re Rhea*, 17 B.R. 789 (Bankr. W.D. Okla. 1982); *In re Samoset Associates*, 14 B.R. 408 (Bankr. D. Me. 1981); *In re Supergrate Open Steel Flooring Co.*, 1 B.R. 660 (Bankr. C.D. Cal. 1979).

**28 U.S.C. §960 (1948) Tax Liability

> Any officers and agents conducting any business under authority of a United States court shall be subject to all Federal, State and local taxes applicable to such business to the same extent as if it were conducted by an individual or corporation.

ARGUMENT II

THE ELEVENTH CIRCUIT HOLDING DOES NOT CONFLICT WITH ASHTON VS. CAMERON COUNTY

The State of Florida argues that the Eleventh Circuit holding conflicts with the ruling of *Ashton vs. Cameron County Water Improvement District*, 298 U.S. 513 (1936).

In *Ashton, supra*, the issue was whether a political subdivison of California, a water district, could seek protection in the Bankruptcy Court by filing a voluntary petition for relief. This Court determined that the power of Congress under the bankruptcy clause did not extend to states or their political subdivisions. Since *Ashton* does not involve a liquidation sale, it does not conflict with the Eleventh Circuit holding.

ARGUMENT III

THE ELEVENTH CIRCUIT HOLDING DOES NOT CONFLICT WITH SWARTS VS. HAMMER

The State of Florida also argues that the Eleventh Circuit decision conflicts with *Swarts vs. Hammer*, 194 U.S. 441 (1904). In *Swarts*, the Trustee had $68,320.00 of funds belonging to the estate in a bank account, and the funds were determined to be subject to property taxes.

The Eleventh Circuit holding and *Swarts, supra*, are not in conflict as *Swarts* deals with personal property in the hands of the Trustee while the business is in operation, *not* liquidation. The distinction is between operating an ongoing business for profit on one hand, and liquidating an inventory at a loss on the other hand. A tax on the latter is a burden to the judicial process:

> A tax may be levied upon specific property in the hands of a trustee in bankruptcy. *Swarts vs. Hammer*, 194 U.S. 441, 24 S.Ct. 695, 48 L.Ed. 1060. But no state is empowered to levy taxes upon the process of the courts of the United States or to impede the officers of court in an essential judicial function. *McCulloch vs. Maryland*, 4 Wheat 316, 432, 17 U.S. 316, 432, 4 L.Ed. 579.

cited in *California State Board of Equalization vs. Goggin*, 191 F.2d 726, 730 (9th Cir. 1951).

ARGUMENT IV

THE HOLDING OF THE ELEVENTH CIRCUIT DOES NOT CONFLICT WITH THE HOLDINGS OF OTHER CIRCUITS

The Petitioner argues that there is a conflict among the Circuit Courts of Appeal on this issue. But there is no conflict.

The Petitioner claims that in the Second, Third, Fifth, Seventh and Eighth Circuits, taxes would be imposed on the bankruptcy Trustee at a liquidation sale. However, the cases cited in support thereof for the Second and Fifth Circuits can be distinguished from the Eleventh Circuit holding: *In Re: Hatfield Construction Co.*,, 494 F.2d 1179 (5th Cir. 1974) and *In Re: Leavy*, 85 F.2d 25 (2nd Cir. 1936). In both these cases, the courts approved of the imposition of a sales tax because the tax was to be imposed on the purchaser at the liquidation sale rather than on the seller/Trustee, and thus there was no burden on the bankruptcy process.

Likewise, the Third Circuit and Seventh Circuit cases cited can be distinguished: *In Re: I.J. Knight Realty Corp.*, 501 F.2d 62 (3rd Cir. 1974) and *Pinkerton vs. United States*,, 73 F.Supp. 590 (S.D. Ill. 1947), *affirmed*, 170 F.2dd 846 (7th Cir. 1948). In the first place, both cases involve the imposition of Federal income taxes not a state tax, and neither case deals with a liquidation sale. Further, *Knight, supra*, deals with a Trustee who received capital gains income generated from a condemnation salle of land and income from interest on insurance proceeds over a seven year period. *Pinkerton, supra*, deals with a Trustee in a State court proceeding,

not a bankruptcy Trustee, who was held responsible for Federal taxes on rental income and capital gains.

The Eighth Circuit case can be distinguished in that it is based on a specific Missouri statute which expressly includes "bankruptcy trustees" within the category of those liable for State unemployment taxes. *State of Missouri vs. Gleick*, 135 F.2d 134 (8th Cir. 1943).

The Eleventh Circuit is not alone in prohibiting the taxation of bankruptcy trustee liquidation sales. The Ninth Circuit also refuses to impose a tax where the Trustee is merely liquidating. *California State Board of Equalization vs. Goggin*, 245 F.2d 44 (9th Cir. 1957) *cert. denied*, 353 U.S. 961 (1957). The Petitioner claims that the Ninth Circuit in *Goggin*, distinguishes liquidation sales of assets other than inventory from liquidation sales of strictly inventory, and imposes a tax only on the former. However, the characterization of the property sold was not a relevant factor in the decision.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

Mary Ellen Shoemaker

by MARY ELLEN SHOEMAKER, ESQ.
REGGIE DAVID SANGER, ESQUIRE
208 S.E. 9th Street
Fort Lauderdale, FL 33316
(305) 463-8547

May 6, 1985

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by U.S. Mail, first-class postage prepaid, to Harold F. X. Purnell, General Counsel, Department of Business Regulation, 725 South Bronough Street, Tallahassee, Florida 32301 this 10 day of May, 1985.

Mary Ellen Shoemaker

by MARY ELLEN SHOEMAKER, ESQ.
REGGIE DAVID SANGER, ESQUIRE